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SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1935

No. 540

THEODORE STITT,

Petitioner,

vs.

RECONSTRUCTION FINANCE CORPORATION.

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT

BRIEF FOR PETITIONER.

THEODORE STITT,
Pro se.

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BRIEF FOR PETITIONER.

Opinion Below.

The opinion of the Circuit Court of Appeals is reported in 79 F. (2d) 187 and is printed in the record (R. 287).

That part relating to the referee's compensation is as follows:

> "The award of $25,000 to the referee was clearly erroneous. We have already shown that the reorganization court was without power to increase allowances fixed by the prior court and that the prior court was limited by the provisions of the Bankruptcy Act. Under Section 40 (a) of that act referees are only entitled to 'a fee of fifteen dollars * * * in each case * * * and twenty-five cents for every proof of claim filed for allowance * * * and from estates which have been administered before them one per centum commission on all moneys disbursed to creditors by the trustee * * *.' Under Section 40 (a) the referee here was limited to a fee of $15 and his filing fees and under Section 72 could not 'in any form or guise * * * receive any other or further compensation.'"

Jurisdiction.

The order of the Circuit Court of Appeals was made July 29, 1935 (R. 295). Petition for rehearing was denied and mandate issued September 18, 1935 (R. 306). The petition for a writ of certiorari was filed October 24, 1935, and was granted December 9, 1935.

The jurisdiction of this Court is invoked under Section 240 (a) of the Judicial Code as amended by Act of Congress February 13, 1925 (U. S. Code, Title 28, Sec. 347).

Question Presented.

Whether a referee is entitled under Sections 77B (i), 40-a and 40-c of the Bankruptcy Act to receive equitable and reasonable compensation for services rendered by him from time of reference of bankruptcy proceeding to time of filing of petition under Section 77B.

Statement.

Petitioner appeals from order of the Circuit Court of Appeals for Second Circuit reversing order of District Court for Eastern District of New York fixing referee's compensation in the sum of $25,000.00. Petition for rehearing was denied.

In view of the addition of Section 77B to the Bankruptcy Act since the commencement of the bankruptcy proceeding, the new interpretation of Section 40 with reference to referee's commissions (*Realty Associates Securities Corporation* v. *O'Connor,* 295 U. S. 295), made since the referee's allowance was fixed by the District Judge, and confirmation of reorganization plan also since the allowance was made, I respectfully submit the following chronological statement:

August 8, 1933:

Allied Owners Corporation adjudicated bankrupt and referred to Referee Stitt. Estate administered for ten months thereafter under referee's supervision.

June 7, 1934:

Section 77B enacted.

June 22, 1934:

Allied Owners Corporation's petition under Section 77B filed and approved. Oscar A. Lewis, Esq., was designated as Special Master on the plan of reorganization, on consummation thereof after its confirmation, and on the adjudication of all large claims. Referee Stitt was designated as Special Master on filing of claims and countersignature of checks.

December 3, 1934:

Realty Associates Securities Corporation, C. C. A. 2nd Cir. 74 F. (2d) 61. Held, that referee's commissions should

be computed on face amount of bonds issued on composition.

March 5, 1935:

Referee filed petition for allowance (R. 188) in the sum of $25,000.00 for services rendered from August 8, 1933, to June 22, 1934, the date of the filing of 77B petition. This amount consisted of $23,977.00 commissions or 35⅖% of full commissions computed at ½% of total amount of undisputed claims and the sum of $1,023.00 for 4,092 claims filed at 25 cents per claim.

March 11, 1935:

Referee's application allowed in full by Judge Inch.

March 20, 1935:

Order to show cause signed by Judge Inch as to why referee's allowance should not be reduced on the application of Reconstruction Finance Corporation, a creditor.

April 29, 1935:

Realty Associates Securities Corporation v. *O'Connor*, 295 U. S. 295. Held, that referee's commissions should be computed on market value of bonds issued on composition.

May 13, 1935:

Order made by Judge Inch denying application of Reconstruction Finance Corporation to reduce referee's allowance (R. 270). Order based on opinion May 8, 1935 (R. 263).

June 13, 1935:

Allied Owners reorganization plan confirmed. No cash is being paid under the plan. Creditors are being paid in

full on the face amount of allowed claims by the issuance of new bonds with deferred maturity and reduced interest to first mortgage bondholders and debenture bondholders, by the issuance of third lien notes to creditors secured by third mortgage and unsecured creditors. Additional security for out-of-town theater mortgage bondholders (R. 298, 303).

Specifications of Error to be Urged.

The Circuit Court of Appeals erred:

(1) In holding that Referee was not entitled to compensation under Sections 77B (i), 40-a and 40-c for ten months' services except $15.00 filing fees and 25 cents for each claim.

(2) In holding that under Section 72 the referee is not entitled to part commissions.

(3) In failing to consider that part of Section 40-a upon which the referee's application for allowance was based together with Sections 77B (i) and 40-c.

Summary of Argument.

Under Section 77B (i) providing for equitable and reasonable compensation for services rendered before petition under Section 77B, the referee was properly allowed an apportioned part of composition commissions provided for under Section 40 (a) and 40 (c) based on the amount to be paid creditors under the 77B reorganization plan.

Equitable and reasonable compensation under Section 77B (i) is measured by and obviously should not exceed an apportioned part of the amount which would have been earned if the estate had been fully administered in the prior proceeding.

Reorganization plan is a composition and a portion of the one-half per cent commissions provided for in Section

40-a is the correct basis for arriving at equitable and reasonable compensation. Under Section 40-c, part commissions are to be paid when reference is revoked before conclusion.

Commissions were actually earned, the referee having rendered substantial services and carried heavy responsibility for ten months in supervising the administration of this estate.

The effect of the decision of the Circuit Court of Appeals is to deprive the referee of all compensation for these services solely by reason of the act of the debtor in filing a petition under Section 77B.

ARGUMENT.

The basis for allowance of part commissions as compensation to the referee is found in Sections 77B (i), 40-a and 40-c.

I.

Equitable and reasonable compensation under Section 77B (i) is measured by and obviously should not exceed an apportioned part of the amount which would have been earned if the estate had been fully administered in the prior proceeding.

Section 77B (i) reads as follows:

> "If a receiver or trustee of all or any part of the property of a corporation has been appointed by a Federal, State, or Territorial court, whether before or after this amendatory act takes effect a petition or answer may be filed under this section at any time thereafter by the corporation, or its creditors as provided in subdivision (a) of this section and if such petition or answer is approved, the trustee or trustees appointed under this section, or the debtor if no trustee is appointed, shall be entitled forthwith to possession of and vested with title to such property, and the

> judge shall make such orders as he may deem equitable for the protection of obligations incurred by the receiver or prior trustee and for the payment of such reasonable administrative expenses and allowances in the prior proceeding as may be fixed by the court appointing said receiver or prior trustee. * * *"

The intention of Congress to make both equitable and reasonable provision for services rendered prior to the 77B proceeding is clear. To deny the referee part commissions for services rendered for a period of ten months prior to the 77B petition, would seem to make a nullity of this section.

The only limitation as to compensation under this section would seem to be by common sense inference that the allowance certainly should not be greater than an apportioned part of that authorized under Section 40. At the same time, it seems also to be apparent that the court could allow less than the compensation provided in Section 40 provided the amount authorized by that section should be considered more than equitable or reasonable.

Even the appellant in the Circuit Court of Appeals suggests that there is a hardship on the referee in denying him any commissions for ten months' services. At page 45 of its brief submitted to that court, the following appears:

> "Incidentally, the hardship, if any, in the instant case, is more apparent than real. The referee in the bankruptcy proceeding has been appointed a Special Master in the reorganization proceeding, and will undoubtedly become entitled to compensation for his services as such Special Master."

The contrary of the foregoing quotation is the fact. Upon the filing of the 77B petition, the referee was relieved of practically all responsibility in that Oscar A. Lewis, Esq., was designated as Special Master in charge of the re-

organization plan and, after its confirmation, was designated Special Master in charge of the consummation thereof. The referee was designated as Special Master on the filing of claims and bonds and his duties have been largely clerical.

At page 9 of its brief in opposition to the granting of writ, respondent again points out that the referee has been appointed a special master under Section 77B.

II.

Reorganization plan is a composition and a portion of the one-half per cent commissions provided for in Section 40a is the correct basis for arriving at equitable and reasonable compensation. Under Section 40c, part commissions are to be paid when reference is revoked before conclusion.

Section 40-a reads as follows:

> "Referees shall receive as full compensation for their services, payable after they are rendered, a fee of fifteen dollars deposited with the clerk at the time the petition is filed in each case, except when a fee is not required from a voluntary bankrupt, and twenty-five cents for every proof of claim filed for allowance, to be paid from the estate, if any, as a part of the cost of administration, and from estates which have been administered before them one per centum commissions on all money disbursed to creditors by the trustee, or one-half of one per centum on the amount to be paid to creditors upon the confirmation of a composition."

It appears from the foregoing that referees are entitled to commissions in two events. If there is a liquidation of the estate, he is to receive one per cent on money disbursed to creditors by the trustee. If there is a composition, he is to receive one-half of one per cent on the amount to be paid to creditors upon confirmation. It is on the latter event that the referee based his application, although the Circuit

Court of Appeals appears to have been under the impression that the referee was asking for commissions of one per cent on monies paid to creditors as in a liquidation.

The word "composition" used in the statute is not restricted to a proceeding under Section 12 of the Bankruptcy Act. A reorganization has been held to be a composition. Matter of *O'Gara Coal Company,* 260 Fed. 742.

Reorganization plan held not distinguishable in principle from composition in upholding constitutional validity of Sections 77 and 77B. *Continental* v. *Chicago,* 294 U. S. 648, 55 S. Ct. 595; *in re Central* (C. C. A. 2d), 75 F. (2d) 257; *Campbell* v. *Allegheny* (C. C. A. 4th), 75 F. (2d) 947. General order XLVIII provides same commissions for referee under Section 74 extension proposal as on a composition.

I have examined all of the reported decisions relating to Section 40. I find no case where commissions have been denied to a referee where there was a distribution to creditors either through liquidation or settlement except one, *in re Stillwell,* 12 F. (2d) 205. There, the referee was guilty of misconduct.

Attention is called to the fact that resort to Section 77B was had at a time when the estate was being administered under the Bankruptcy Act. Although the corporation is now known as a debtor, there is still in effect, an order of the District Court adjudicating the corporation a bankrupt. There was no change in the size or condition of the estate when it passed to the process of reorganization under Section 77B except that the corporation became known as a debtor instead of a bankrupt. No part of the estate was disbursed or paid out to anyone at the time that the 77B petition was filed and approved. The same bankruptcy trustees were designated as debtor trustees and continued the administration of the estate including the conduct of the business of the corporation.

Section 40-c.

Section 40-c reads as follows:

> "In the event of the reference of a case being revoked before it is concluded, and when the case is specially referred, the judge shall determine what part of the fee and commissions shall be paid to the referee."

The effect of the approval of the 77B petition was to revoke the reference.

I find no reported decisions construing this section. It speaks for itself and says plainly that the referee is to have part commissions where the reference is revoked prior to a distribution either by dividend or composition.

Section 72.

Section 72 reads as follows:

> "That neither the referee, receiver, marshal, nor the trustee shall in any form or guise receive, nor shall the court allow him, any other or further compensation for his services than that expressly authorized and prescribed in this Act."

This section is cited in the decision of the Circuit Court of Appeals as authority for denying the referee any commissions. The section is prohibitive as to any other or further compensation than that provided under Section 40-a. It does not take anything away from Section 40-a. Commissions are specifically provided for in Section 40-a. Commissions are plainly not "other or further compensation."

Inasmuch as the Circuit Court of Appeals reversed the orders providing for compensation by way of commissions on the ground that there is no authority in law for any commissions, the question of the amount on which commissions are to be computed, will not be discussed here. There

is no finding that the amount allowed by the District Court was excessive or incorrectly computed. A discussion of the method of computation of commissions is in the referee's petition for rehearing (R. 296).

In re Le Bolt & Co., N. D. Illinois (unreported) (appendix), was followed by referee in computing his commissions.

III.

Commissions were actually earned, the referee having rendered substantial services and carried heavy responsibility for ten months in supervising the administration of this estate.

The effect of the decision of the Circuit Court of Appeals is to deprive the referee of all compensation for these services solely by reason of the act of the debtor in filing a petition under Section 77B.

The extent of the services rendered by the referee are indicated in his petition for allowance at (R. 190). Though referee's compensation is not on a basis of *quantum meruit*, for his own satisfaction, he wishes to have the record clear that he petitioned for compensation for work of importance actually rendered as an officer of the court in charge of a $14,000,000.00 corporation operating seven "first-run" motion pictures theaters.

The enactment of Section 77B provided a new method for settlement of debts with creditors. It allows this method to be availed of at any time during a pending bankruptcy proceeding. The decision of the Circuit Court of Appeals holds that a referee is entitled to no compensation by way of commissions no matter how long the estate has been under his supervision when superseded by a petition under Section 77B.

If this is the law (and Sections 77B (i), 40-a and 40-c seem to the contrary), it would be a simple matter for any bankrupt, creditor or stockholder to deprive a referee, who has not been satisfactory to them, of fair compensation by the device of filing a petition under Section 77B.

It is against the public interest for a referee, as to his compensation, to be placed in the complete control and at the whim or fancy of a bankrupt, creditor or stockholder.

The decision of the Circuit Court of Appeals construes Section 77B (i), a new statute which has never been construed by this Court. The clear intent of that section to provide equitable and reasonable compensation for services rendered prior to the filing of Section 77B petition is nullified by this decision.

Conclusion.

Petitioner has shown clear warrant of law in Sections 77B (i), 40-a and 40-c of the Bankruptcy Act for the compensation allowed by the District Court.

In denying compensation, the Circuit Court of Appeals failed to consider the basis in fact and in law relied upon in referee's petition.

The order of the Circuit Court of Appeals should be reversed.

Dated, Brooklyn, New York, December 31, 1935.

THEODORE STITT,
Petitioner.

APPENDIX.

UNITED STATES DISTRICT COURT, NORTHERN DISTRICT OF ILLINOIS.

Referee's Report, 55997 Bankruptcy, 56413 Reorganization.

In re Lebolt & Co., Debtor.

On May 21, 1934, a voluntary petition in bankruptcy was filed by the bankrupt, and thereafter, on May 23, 1934, an order of adjudication was entered and the cause was generally referred to me as Referee in Bankruptcy. Various proceedings were had thereafter, including calling of first meeting of creditors and continuing same from time to time until the proceedings were suspended by the filing by the bankrupt of a petition under Sections 77-A and 77-B of the Bankruptcy Act. That petition was filed June 29, 1934, and the petition was approved as properly filed on June 30, 1934. On August 13, 1934, an order was entered generally referring the said proceedings under Section 77-B to me as Special Master.

Proceedings have been had pursuant to said reference which resulted in the entry by me as Special Master of an order, among other things, approving the plan of reorganization, which distributes to creditors approximately $480,000.

It is necessary that the compensation of the referee be fixed by your Honor in both cases. The order entered by me as Special Master in the proceedings under Section 77-B, which is No. 56,413 in this Court, suggests that the fair and reasonable compensation of the referee as Special Master in said 77-B proceeding is $1,200.67 and that $75.00 in addition represents the actual and necessary expenses of the referee as Special Master in connection with said reference in said cause.

Sub-section c of Section 40 of the Bankruptcy Act provides: "In the event of the reference of a case being revoked before it is concluded, * * *" the Judge shall determine what part of the fee and commissions shall be paid to the referee.

The filing of the petition by the bankrupt under Sections 77-A and B, and the approval of the petition as properly filed, caused the court to have exclusive jurisdiction of all the property of the bankrupt wherever located. That proceeding had the effect of revoking the order of reference in the bankruptcy case filed May 21, 1934.

In arriving at the amount of compensation that should be allowed to the referee in the bankruptcy proceeding and to the Special Master in the proceeding for relief under Sections 77-A and B, it was thought that it would be fair to the debtor corporation to consider the two proceedings as really one. In other words, it would not be fair to fix the compensation in one proceeding without regard to the compensation to be fixed in the other. Therefore, the result of the two proceedings is, in effect, a composition between the debtor and its creditors.

Sub-section a of Section 40 provides for the compensation to the referee in case of composition as "one-half of one per cent on the amount to be paid to creditors * * *." As the amount to be paid to creditors is approximately $480,000, and one-half of one per cent of the sum actually to be paid is $2,401.34, that is the amount which has been considered by me as fair and reasonable compensation for the referee's and special master's services in the two cases.

The method pursued finds support in the action of the Supreme Court in providing for compensation to the referee under Section 74 of the Bankruptcy Act which relates to relief of individuals. Section 74 provides for references to the referee. It was, however, silent as to compensation in the event an extension proposal was confirmed. To take care of that situation, the Supreme Court, pursuant to the Bankruptcy Act, promulgated General Order 48, which, among other things, provides (clause 4): "For the purposes of computing the commissions of the referee and of the custodian or receiver, the term 'composition' as used in Sections 40 and 48 of the act shall be deemed to include an extension proposal, and the amount of the debts whose maturity is to be extended thereunder and of the debts, if any, to be paid in full on the confirmation, shall be deemed

to be 'the amount to be paid creditors' within the meaning of said section."

Having reached the conclusion that said sum of $2,401.34 is the fair and reasonable compensation to the referee and Special Master in both proceedings, I have further considered the question as to what should be allowed in each of the proceedings, and I believe that, considering the amount and character of work done, that fair division is to divide it equally.

I therefore respectfully ask that your Honor fix the compensation of the referee in this proceeding at $1,200.67 and the actual and necessary expenses at $25.00, and in the proceedings under Section 77-B the compensation of the Special Master at $1,200.67 and the actual and necessary expenses at $75.00.

Dated September 20, 1934.

EDMUND D. ADCOCK,
Referee.

Report affirmed by District Judge, September 20, 1934.